Supreme Court, U.S.
FILED
051335 APR 14 2006
OFFICE OF THE CLERK

No. 05-

IN THE

Supreme Court of the United States

DARRYL S. LADDIN, AS TRUSTEE OF THE ETS CREDITORS' LITIGATION TRUST,
Petitioner,

v.

RELIANCE TRUST COMPANY, PENSCO, INC. AND COMMUNITY NATIONAL BANK,
Respondents.

Petition for Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

---

PETITION FOR WRIT OF CERTIORARI

ALLEN I. HIRSCH *
DARRYL S. LADDIN
FRANK N. WHITE
ARNALL GOLDEN GREGORY LLP
171 17th Street N.W.
Suite 2100
Atlanta, Georgia 30363
(404) 873-8500

* Counsel of Record

Attorneys for Petitioner, Darryl S. Laddin, as Trustee of the ETS Creditors' Litigation Trust

WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D.C. 20001

QUESTIONS PRESENTED FOR REVIEW

1. Whether the personal, equitable defense of *in pari delicto* is assertable against a bankruptcy trustee who has succeeded to the interests of a debtor pursuant to 11 U.S.C. § 541(a), where the debtor and alleged wrongdoer has been eliminated and any causes of action successfully prosecuted by the trustee will inure solely to the benefit of innocent investors and other creditors of the bankruptcy estate.

2. Whether, in any case or context, the *in pari delicto* defense applies to causes of action arising under the federal Racketeer Influenced and Corrupt Organizations ("RICO") Act, 18 U.S.C. § 1961, *et seq.*

3. Whether, even if assertable against a wrongdoer, the *in pari delicto* defense applies to RICO claims brought by a bankruptcy trustee, given the strong policies of compensation and deterrence embodied in the RICO Act and equitable principles favoring distributions to creditors embodied in the United States Bankruptcy Code, 11 U.S.C. § 101, *et seq.*

PARTIES

The caption of this Petition contains the names of all remaining parties to this action. The original plaintiff in this action was the Official Committee of Unsecured Creditors of PSA, Inc., *et al.* (the "Committee"). The plan of reorganization confirmed in the underlying bankruptcy case, *In re PSA, Inc., et al.*, in the United States Bankruptcy Court for the District of Delaware, Case No. 00-3570 (JCA), subsequently created the ETS Creditors' Litigation Trust (the "Trust"), of which the Petitioner was appointed as Trustee. All interests in any claims or causes of action held by the bankruptcy estate were thus transferred from the Committee to the Trust, and Petitioner was substituted for the Committee as the plaintiff in this action. The case was also transferred from the Bankruptcy Court to the United States District Court for the Northern District of Georgia, Atlanta Division. All Defendants in the case other than the Respondents entered into settlements with the Petitioner while the case was pending in the courts below, and therefore are no longer parties to these proceedings.

CORPORATE DISCLOSURE STATEMENT

The Petitioner does not have any parent corporation or stockholders, and therefore has nothing to disclose pursuant to Supreme Court Rule 29.6.

TABLE OF CONTENTS

	Page
QUESTIONS PRESENTED FOR REVIEW	i
PARTIES	ii
CORPORATE DISCLOSURE STATEMENT	ii
TABLE OF AUTHORITIES	v
OPINIONS BELOW	1
JURISDICTION	2
STATUTES INVOLVED	2
STATEMENT OF THE CASE	2
REASONS FOR GRANTING THE WRIT	8
I. This Case Presents The Court With An Issue Of Unquestionable, National Importance, And An Opportunity To Reverse The Trend Of Incorrect, Ill-Founded And Roundly Criticized Decisions Rendered By The Circuit Courts To Date	8
A. The Eleventh Circuit's ruling that Section 541 requires application of the *in pari delicto* defense to a bankruptcy trustee has no basis in the plain language of the statute, and is directly inconsistent with Congress' clear and unequivocal expression of its intent	9
B. The Eleventh Circuit's ruling that Section 541 is so "unambiguous" as to prohibit consideration of its legislative history creates a split in the Circuits, and a departure from prior rulings by this Court, on that issue	12

TABLE OF CONTENTS—Continued

Page

II. This Case Creates A Split In The Federal Courts On Application Of The *In Pari Delicto* Defense To RICO Claims Generally, And Presents That Issue To This Court For A Definitive Ruling 16

III. The Results In This Case, And In The Prior Circuit Court Decisions Applying *In Pari Delicto* To Bankruptcy Trustees, Betray The Equitable Principles Embodied In The Bankruptcy Code And Conflict With The Manner—Accentuating Flexibility In The Service Of Equity Rather Than Rote Application—In Which This Court And The Other Federal Courts Have Consistently Directed Section 541 And Other Provisions Of The Bankruptcy Code To Be Administered 18

CONCLUSION 24

APPENDIX A 1a

APPENDIX B 13a

TABLE OF AUTHORITIES

CASES Page

Allapattah Servs., Inc. v. Exxon Corp., 362 F.3d 739 (11th Cir. 2004) 14
Am. Nat'l Bank v. MortgageAmerica Corp. (In re MortgageAmerica Corp.), 714 F.2d 1266 (5th Cir. 1983) 14
Anstine v. Alexander, 128 P.3d 249 (Colo. App. 2005) 21
Bateman Eichler, Hill Richards, Inc. v. Berner, 472 U.S. 299, 105 S. Ct. 2622 (1985) 11, 17, 21
Computer Commc'n, Inc. v. Codex Corp. (In re Computer Commc'n, Inc.), 824 F.2d 725 (9th Cir. 1987) 14
Exxon Corp. v. Oxxford Clothes, Inc., 109 F.3d 1070 (5th Cir. 1997) 12
Garner v. Strauss (In re Garner), 952 F.2d 232 (8th Cir. 1991) 14
Harper v. American Tel. and Tel. Co., 54 F. Supp. 2d 1371 (S.D. Ga. 1999) 16
Hrisomalos v. Smith, 600 N.E.2d 1363 (Ind. Ct. App. 1992) 12
Huber v. Danning (In re Thomas), 147 B.R. 526 (9th Cir. 1992) 15
In re Combustion Eng'g, Inc., 391 F.3d 190 (3d Cir. 2004) 15
In re National Mtg. Equity Sec. Litig., 636 F. Supp. 1138 (C.D. Cal. 1986) 17
In re Paeplow, 972 F.2d 730 (7th Cir. 1992) 14
In re S.W. Citizens' Org. for Poverty Elimination, 91 B.R. 278 (Bankr. D.N.J. 1988) 15
In re Southern Star Foods, Inc., 144 F.3d 712 (10th Cir. 1998) 14
In re Village Rathskeller, Inc., 147 B.R. 665 (Bankr. S.D.N.Y. 1992) 15

TABLE OF AUTHORITIES—Continued

Page

Johnson, Blakely, Pope, Bokor, Ruppel & Burns, P.A. v. Alvarez (In re Alvarez), 224 F.3d 1273 (11th Cir. 2000) 13

Kokoszka v. Belford, 417 U.S. 642, 94 S. Ct. 2431 (1974) 20

L.R.S.C. Co. v. Rickel Home Ctrs., Inc. (In re Rickel Home Ctrs., Inc.), 209 F.3d 291 (3d Cir. 2000) 26

Laddin v. Edwards (In re PSA, Inc.), 437 F.3d 1145 (11th Cir. 2006) 12, 17, 19

McNamara v. PFS (In re The Personal & Bus. Ins. Agency), 334 F.3d 239 (3d Cir. 2003) 21

Miller v. Shallowford Cmty. Hosp. Inc., 767 F.2d 1556 (11th Cir. 1985) 13

*Nomura Sec. Int'l, Inc. v. E*Trade Sec., Inc.*, 280 F. Supp. 2d 184 (S.D.N.Y. 2003) 12

O'Melveny & Myers v. FDIC, 512 U.S. 79, 114 S. Ct. 2048 (1994) 16

Official Comm. of Unsecured Creditors v. R.F. Lafferty & Co., Inc., 267 F.3d 340 (3d Cir. 2001) 10, 14, 23

Page v. Edmunds, 187 U.S. 596, 23 S. Ct. 200 (1903) 20

Perma Life Mufflers, Inc. v. International Parts Corp., 392 U.S. 134, 88 S. Ct. 1981 (1968) 17, 21

PM Denver, Inc. v. Porter (In re Porter McLeod, Inc.), 231 B.R. 786 (D. Colo. 1999) 21

Pyrodyne Corp. v. Pyroteronics Corp., 847 F.2d 1398 (9th Cir. 1988) 12

Resolution Trust Corp. v. Associated Gulf Contractors, Inc., 622 A.2d 1324 (N.J. Super. Ct. App. Div. 1993) 12

TABLE OF AUTHORITIES—Continued

	Page
Rodgers v. County of Monroe (In re Rodgers), 333 F.3d 64 (2d Cir. 2003)	13
Schacht v. Brown, 711 F.2d 1343 (7th Cir. 1983)	16, 17
Scholes v. Lehmann, 56 F.3d 750 (7th Cir. 1995)	23
SEC v. Edwards, 540 U.S. 389 (2004)	2
Segal v. Rochelle, 382 U.S. 375, 86 S. Ct. 511 (1966)	19, 20
Sender v. Buchanan (In re Hedged-Investments Assocs.), 84 F.3d 1281 (10th Cir. 1996)	10, 14
Shumate v. Patterson, 943 F.2d 362 (4th Cir. 1991)	14
T & B Scottdale Contractors, Inc. v. United States, 866 F.2d 1372 (11th Cir. 1989)	13
Tolz v. Proskauer Rose LLP (In re Fuzion Tech. Group, Inc.), 332 B.R. 225 (S.D. Fla. 2005)	9, 12, 22, 23
Tringali v. Hathaway Mach. Co., Inc., 796 F.2d 553 (1st Cir. 1986)	13
United States v. Inslaw, Inc., 932 F.2d 1467 (D.C. Cir. 1991)	14
United States v. Whiting Pools, Inc., 462 U.S. 198 (1983)	13
Weingarten Nostat, Inc. v. Serv. Merch. Co., Inc., 396 F.3d 737 (6th Cir. 2005)	14

STATUTES

11 U.S.C. § 541(a)	2, 9
11 U.S.C.A. § 541 note (West 2004) (Legislative Statements); 124 CONG. REC. 32,399 (1978)	11, 15
11 U.S.C.A. § 541 note (West 2004) (Revision Notes and Legislative Reports—1978 Acts); 1978 U.S.C.C.A.N. 5963	9, 10, 19
18 U.S.C. §§ 1962(c)-(d)	6

TABLE OF AUTHORITIES—Continued

OTHER AUTHORITIES — Page

5 COLLIER ON BANKRUPTCY ¶ 541.04 (15th rev. ed. 2004) 11, 15

Gerald L. Baldwin, *In Pari Delicto Should Not Bar a Trustee's Recovery*, 23 AM. BANKR. INST. J. 8 (Oct. 2004) 9

Jeffrey Davis, *Ending the Nonsense: The In Pari Delicto Doctrine Has Nothing to Do with What is § 541 Property of the Bankruptcy Estate*, 21 EMORY BANKR. DEV J. 519 (Summer 2005) 8, 11

Making Sense of the In Pari Delicto Defense: "Who's Zoomin' Who?" 23 No. 11 BANKR. LAW LETTER 1 (Nov. 2003) 9

Robert T. Kugler, *The Role of Imputation and In Pari Delicto in Barring Claims Against Third Parties*, 1 No. 14 ANDREWS BANKR. LIT. REP. 13 (2004) 9

Tanvir Alam, *Fraudulent Advisors Exploit Confusion in the Bankruptcy Code: How In Pari Delicto Has Been Perverted to Prevent Recovery for Innocent Creditors*, 77 AM. BANKR. L.J. 305 (Summer 2003) 8

IN THE

Supreme Court of the United States

No. 05-___

DARRYL S. LADDIN, AS TRUSTEE OF THE
ETS CREDITORS' LITIGATION TRUST,
Petitioner,

v.

RELIANCE TRUST COMPANY, PENSCO, INC. AND
COMMUNITY NATIONAL BANK,
Respondents.

**Petition for Writ of Certiorari to the
United States Court of Appeals
for the Eleventh Circuit**

PETITION FOR WRIT OF CERTIORARI

Darryl S. Laddin, as Trustee of the ETS Creditors' Litigation Trust, respectfully petitions This Honorable Court for a writ of certiorari to review the judgment of the United States Court of Appeals for the Eleventh Circuit in this case.

OPINIONS BELOW

The opinion of the United States District Court for the Northern District of Georgia granting the Respondents' motion to dismiss (attached as Appendix A hereto) is not reported. The opinion of the United States Court of Appeals for the Eleventh Circuit affirming the District Court's dismissal of claims against the Respondents (attached as Appendix B hereto) is reported at 437 F.3d 1145 (11th Cir. 2006).

JURISDICTION

The order of the Eleventh Circuit at issue in this Petition was entered on January 30, 2006. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTES INVOLVED

Section 541(a) of the United States Bankruptcy Code, 11 U.S.C. § 541(a), provides, in pertinent part:

> The commencement of a case under . . . this title creates an estate. Such estate is comprised of . . . all legal and equitable interests of the debtor in property as of the commencement of the case.

STATEMENT OF THE CASE

The facts relevant to this appeal are not complicated.[1] In 1994, Charles Edwards formed ETS Payphones, Inc. ("ETS"), with the initial intent of purchasing a small number of payphones to operate himself. Unfortunately, however, he shortly conceived of an ill-fated business plan for ETS that ultimately deteriorated into a classic Ponzi scheme. Touted under the slogan "Opportunity doesn't always knock . . . sometimes it rings," the scheme ultimately bilked thousands of investors—many elderly or retired—out of hundreds of millions of dollars, and left ETS with an insurmountable $400 million in debt and doomed to bankruptcy. As correctly observed by Justice O'Connor in reference to Edwards's catch phrase "opportunity rings," for the 10,000 people who invested a total of $300 million in the scheme, "sometimes it hangs up."[2]

---

[1] Because this appeal stems from successful motions to dismiss, the Court must accept as true the allegations in the Petitioner's complaint. *See, e.g., SEC v. Edwards*, 540 U.S. 389, 391 (2004).

[2] *Edwards*, 540 U.S. at 391.

The essence of the ETS business plan involved the sale of payphones to the public as a vehicle for investment. Each payphone was offered for sale with an agreement that the purchaser lease it back to ETS for a fixed monthly payment, giving the purchaser a guaranteed annual return of 14 or 15 percent on his investment. Remarkably, ETS guaranteed this return regardless of the location or actual income of the payphone.[3] Not surprisingly, thousands of investors bought the pitch. Indeed, it appeared to be a no-lose proposition. Predictably, however, since the rate of return guaranteed by ETS had no basis in the revenue actually generated by the payphones, and the entire plan ignored the advent of cell phones, the payphones eventually failed to generate sufficient revenue for ETS to make the monthly payments required by the leaseback agreements. As a result, in classic Ponzi fashion, ETS inevitably began to depend on funds from new investors to meet its obligations to prior investors. The ever-deepening insolvency of the company, however, was ignored. Instead, Edwards engaged ETS in financial deceptions to cover up the scheme and stepped up the influx of new investors by selling thousands of payphones that did not even exist.[4]

Edwards, of course, did not execute this scheme all by himself. In fact, he had numerous co-conspirators. Among these were marketing professionals who, fully aware of the true nature of the business plan and ETS's financial condition, promoted and marketed the sale and leaseback of the payphones. A nationwide network of agents and brokers

---

[3] Accordingly, for example, a payphone owner whose phone was located at Atlanta's Hartsfield-Jackson International Airport and generated $1,000 per month in coin revenue was promised the same rate of return as the owner whose phone was located behind a dilapidated service station in the middle of the desert and generated only $1 per month.

[4] ETS ultimately sold approximately 13,000 more payphones than it actually owned.

further assisted him in the sale of the phones to the investing public. Like the marketing professionals, many of these agents and brokers continued to earn significant commissions promoting and selling ETS's product long after becoming aware of the fraudulent nature of the scheme.[5] While seemingly extraordinary, tactics of this nature were well worth the effort: ETS's agents and marketing professionals earned substantial commissions (no less than $200 million in the aggregate), in addition to lavish vacations and other prizes bestowed by Edwards (through ETS).

The final—and probably most important—component of ETS's marketing and sales machine was a group of Individual Retirement Account ("IRA") custodians. These IRA custodians significantly increased the scale of the scheme by reaching a whole new category of investors—elderly retirees. Essentially, the IRA custodians provided a mechanism by which these people could easily transfer all or a portion of their savings (often their entire life savings) from their existing IRA accounts to a new IRA account for conversion into ETS payphone investments. Specifically, an ETS agent would contact a potential investor who would show interest in the payphone investment but would be unable to purchase the phone because of the lack of available funds. The agent would then ask whether the investor had money in a retirement account. If so, the agent would describe the mechanism by which some or all of the funds from the investor's existing IRA could be transferred into a new IRA for the purpose of buying payphones. The investor would then sign a preprinted form enabling the IRA custodians to transfer the funds. The IRA custodians would then facilitate the conversion of IRA funds into payphone investments, and often

---

[5] One such agent, John Prokop, was an original defendant in this case. The Petitioner settled all claims against Prokop while the case was on appeal in the Eleventh Circuit, however, and thus Prokop is no longer a party to these proceedings.

even sign the lease agreement on behalf of the individual investor.

Respondents Reliance Trust Company, PENSCO, Inc. and Community National Bank were the three principal IRA custodians[6] integral to the perpetuation of the scheme, and had knowledge of the scheme while assisting in its execution. Like the marketing professionals and agents, the IRA Custodians benefited greatly from their participation in the plan, through the payment of various fees and the increase in assets they were able to hold out to the public as being under their management.

As with all Ponzi schemes, the payphone scheme finally crashed, forcing ETS and related entities to file Chapter 11 bankruptcy on September 11, 2000.[7] In the wake of the crash, Edwards was removed from his position as President, CEO, and sole shareholder of ETS, and was ultimately indicted and convicted under an 82-count federal indictment.[8]

The victims of the scheme are two-fold: (1) the investors—typically elderly or retired individuals who lost most, if not all, of their life savings, and (2) ETS itself. Although the remaining, legitimate portion of ETS's payphone business

---

[6] Hereafter, Reliance, PENSCO, and Community National Bank are referred to collectively as the "IRA Custodians."

[7] The bankruptcy case involves a number of debtors, including ETS Payphones, Inc., PSA, Inc., ETS Vending, Inc., and other related entities. The case is styled *In re PSA, Inc., a Delaware Corporation, and Affiliates*, Case No. 00-3570 (JCA), in the United States Bankruptcy Court for the District of Delaware.

[8] *See United States v. Edwards*, Criminal Indictment No. 1:04-CT-329, in the United States District Court for the Northern District of Georgia, Atlanta Division; *id.*, Judgment In A Criminal Case entered March 8, 2006. Edwards and certain other ETS insiders were among the original defendants in this case. The Petitioner has since settled his claims against those individuals, however, and thus they, too, are no longer parties to this case.

was salvaged as part of a plan of reorganization, the value of the reorganized business is less than five percent (5%) of the losses inflicted upon the victims. These victims comprise the overwhelming majority of the creditor body in the bankruptcy case.

This case arose in the course of the ETS bankruptcy case. The Joint Plan of Reorganization confirmed by the Bankruptcy Court created the ETS Creditors' Litigation Trust, and the Court appointed Petitioner Darryl S. Laddin as Trustee. The Petitioner then pursued litigation against various defendants, including Respondents, the IRA Custodians.

In his Third Amended Complaint in this action, the Petitioner asserted claims against the Respondents for, *inter alia*, violations of the RICO Act.[9] Each of the IRA Custodians brought a motion to dismiss, challenging the Petitioner's standing to assert the claims and asserting the affirmative defense of *in pari delicto*. The district court granted the motion and dismissed the RICO claims against all of the Respondents.[10] In its ruling, the district court rejected the Respondents' standing arguments, but applied the defense of *in pari delicto* to bar the Petitioner's RICO claims.

Petitioner appealed, *inter alia*, the district court's dismissal of his RICO claims to the Eleventh Circuit. Petitioner contended (1) that Section 541(a) of the United States Bankruptcy Code, 11 U.S.C. § 541(a), does not mandate application of the personal, equitable defense of *in pari delicto* against a bankruptcy trustee, barring his claims against wrongdoing third parties to the detriment of innocent investors and other creditors of the estate; (2) that, in any event, the *in pari delicto* defense does not apply to causes of action arising under the RICO Act; and (3) that, even if the *in*

---

[9] 18 U.S.C. §§ 1962(c)-(d).

[10] *See* Exhibit A hereto.

pari delicto defense does bar RICO claims brought by a wrongdoer, it does not apply to RICO claims brought by a bankruptcy trustee, given the strong policies of compensation and deterrence embodied in the RICO Act and equitable principles favoring distributions to creditors embodied in the Bankruptcy Code.

In its order on appeal,[11] the Eleventh Circuit affirmed the district court's dismissal of the RICO claims against the Respondents. The Eleventh Circuit reasoned that the express terms of Section 541(a) of the Bankruptcy Code subject a bankruptcy trustee to any and all affirmative defenses—including such personal, equitable defenses as *in pari delicto*—that would have been assertable against the debtor. Characterizing the terms of Section 541(a) as "unambiguous," the Eleventh Circuit refused to consider language in the legislative history expressly indicating that Congress intended precisely to the contrary. The Eleventh Circuit also noted that all of the other Circuit Courts of Appeals that have addressed the issue to date have reached the same conclusion, and dismissed the chorus of recent commentators—discussed *infra*—who insist that Section 541(a) in no way requires a bankruptcy trustee to be subject to the *in pari delicto* defense, and that the prior decisions of courts to the contrary are unnecessary, unjust and inequitable. Finally, the Eleventh Circuit determined that the *in pari delicto* defense is applicable to RICO claims, in particular, that are asserted by a co-conspirator or co-wrongdoer, and thus also bars claims asserted by a bankruptcy trustee who has succeeded to the interests of such a party under Section 541(a).

---

[11] *See* Exhibit B hereto.

REASONS FOR GRANTING THE WRIT

I. This Case Presents The Court With An Issue Of Unquestionable, National Importance, And An Opportunity To Reverse The Trend Of Incorrect, Ill-Founded And Roundly Criticized Decisions Rendered By The Circuit Courts To Date.

This case presents the Court with the opportunity to issue the definitive ruling on an issue of first impression and profound, national importance—the applicability of the *in pari delicto* defense to an innocent bankruptcy trustee—and to correct, once and for all, the consistently unjust and ill-founded rulings issued by the Eleventh Circuit here, and indeed by all of the Circuit Courts that have addressed the question to date. As a result of these rulings, a bankruptcy trustee is currently powerless to pursue claims against parties who aided and abetted wrongful acts committed by now-banished principals and agents of a debtor, even when the sole beneficiaries of such claims would be the innocent victims of the wrongdoing. Countless numbers of innocent creditors, in any case where the insolvency of the debtor was caused by the fraudulent acts of its principals, are thus denied their only potential source for any recovery whatsoever.

To add insult to injury, this result is not even mandated under the applicable provision of the Bankruptcy Code. As explained herein, and contrary to the conclusion reached below, Congress has made it abundantly clear that Section 541 of the Code does not require application of the *in pari delicto* defense to a bankruptcy trustee, barring his claims against wrongdoing third parties to the detriment of innocent investors and other creditors of the estate. For this reason, a growing chorus of commentators,[12] and at least one bank-

---

[12] *See* Jeffrey Davis, *Ending the Nonsense: The In Pari Delicto Doctrine Has Nothing to Do with What is § 541 Property of the Bankruptcy Estate*, 21 EMORY BANKR. DEV J. 519 (Summer 2005); Tanvir Alam,

ruptcy judge,[13] have harshly criticized the prior appellate rulings on the issue and called for them to be overturned. With this case, and in one fell swoop, the Court can do just that.

A. The Eleventh Circuit's ruling that Section 541 requires application of the *in pari delicto* defense to a bankruptcy trustee has no basis in the plain language of the statute, and is directly inconsistent with Congress' clear and unequivocal expression of its intent.

Under Section 541 of the Bankruptcy Code, the filing of a bankruptcy petition creates an estate. The estate is comprised of "all legal or equitable interests of the debtor in property as of the commencement of the case."[14] As the legislative history of Section 541 reflects, causes of action belonging to the debtor fall within this definition.[15] And, as a general proposition, Section 541 "is not intended to expand the debtor's rights against others more than they exist at the commencement of the case."[16]

Fraudulent Advisors Exploit Confusion in the Bankruptcy Code: How In Pari Delicto Has Been Perverted to Prevent Recovery for Innocent Creditors, 77 AM. BANKR. L.J. 305 (Summer 2003); Gerald L. Baldwin, *In Pari Delicto Should Not Bar a Trustee's Recovery*, 23 AM. BANKR. INST. J. 8 (Oct. 2004); *Making Sense of the In Pari Delicto Defense: "Who's Zoomin' Who?"* 23 No. 11 BANKR. LAW LETTER 1 (Nov. 2003); Robert T. Kugler, *The Role of Imputation and In Pari Delicto in Barring Claims Against Third Parties*, 1 No. 14 ANDREWS BANKR. LIT. REP. 13 (2004).

[13] *Tolz v. Proskauer Rose LLP (In re Fuzion Tech.Group, Inc.)*, 332 B.R. 225 (S.D. Fla. 2005).

[14] 11 U.S.C. § 541(a).

[15] 11 U.S.C.A. § 541 note (West 2004) (Revision Notes and Legislative Reports—1978 Acts); 1978 U.S.C.C.A.N. 5963, 6323-24.

[16] *Id.*

Relying on this legislative history and the statute's phrase "as of the commencement of the case," many courts, including the district and appellate courts in this case, have construed Section 541 as requiring a blind application to the bankruptcy trustee of all defenses to which the debtor would have been subject under non-bankruptcy law as of the moment of bankruptcy.[17] This construction is incorrect, however, for many reasons, not the least of which is that the bankruptcy court is a court of equity, and equity is not served by applying defenses personal to the debtor to bar a trustee from pursuing claims to the detriment of innocent victims and the benefit of wrongdoers. Section 541 does not mandate such a result.

Like certain other courts, the lower courts in this case felt bound by the perceived restrictions of Section 541, based on the legislative history limiting the trustee to "no greater rights than the debtor himself had."[18] Significantly, however, Section 541's legislative history also expressly states that defenses that are "personal against the debtor" are *not* effective against the estate:

> Thus, as section 541(a)(1) clearly states, the estate is comprised of all legal or equitable interests of the debtor in property as of the commencement of the case. To the extent such an interest is limited in the hands of the debtor, it is equally limited in the hands of the estate

---

[17] *See, e.g., Sender v. Buchanan (In re Hedged-Investments Assocs.)*, 84 F.3d 1281, 1285-86 (10th Cir. 1996); *Official Comm. of Unsecured Creditors v. R.F. Lafferty & Co., Inc.*, 267 F.3d 340, 356 (3d Cir. 2001).

[18] *See* 11 U.S.C.A. § 541 note (West 2004) (Revision Notes and Legislative Reports—1978 Acts; 1978 U.S.C.C.A.N. 5963, 6323-24.

> *except to the extent that defenses which are personal against the debtor are not effective against the estate.*[19]

Although this portion of the legislative history has been inexplicably overlooked by most courts, its validity is recognized by numerous, highly respected authorities on bankruptcy law and at least one court.[20]

At a minimum, the seemingly absolute limit on the trustee's power to assert a claim—"He could take no greater rights than the debtor himself had"—is clearly contradicted by the more specific mitigating language "except to the extent that defenses which are personal against the debtor are not effective against the estate." By ignoring or—in the case of the Eleventh Circuit here—refusing to consider the second phrase, courts have found the legislative history more restrictive than it really is. Hence, under a complete reading of Section 541's legislative history, a bankruptcy trustee is subject to the same defenses to which the debtor is at the moment of bankruptcy, *except* those defenses that are "personal" against the debtor. Indeed, the Latin phrase *in pari delicto* refers to a plaintiff's participation in the same wrongdoing as the defendant.[21] It is a defense that prevents a

---

[19] 11 U.S.C.A. § 541 note (West 2004) (Legislative Statements) (emphasis added); 124 CONG. REC. 32,399 (1978).

[20] *See, e.g.*, 5 COLLIER ON BANKRUPTCY ¶ 541.04 (15th rev. ed. 2004) ("To the extent an interest is limited in the hands of the debtor, it is equally limited as property of the estate *except to the extent that defenses which are personal against the debtor are not effective against the estate.*" (emphasis added)); Jeffrey Davis, *Ending the Nonsense: The In Pari Delicto Doctrine Has Nothing to Do with What is § 541 Property of the Bankruptcy Estate*, 21 EMORY BANKR. DEV. J. 519, 538-39 (Summer 2005) (same). *See also In re Fuzion Tech.*, 332 B.R. at 231-232 (same).

[21] The doctrine of *in pari delicto* has its root in the Latin phrase, *in pari delicto potior est conditio defendentis*, which translates to mean, "in the case of equal or mutual fault, the position of the defending party is the better one." *Bateman Eichler, Hill Richards, Inc. v. Berner*, 472 U.S. 299, 306, 105 S. Ct. 2622, 2626 (1985).

plaintiff who has participated in wrongdoing from recovering damages resulting from the wrongdoing.[22] Accordingly, the primary focus of the defense is on the personal malfeasance of the individual seeking to recover damages. This is the epitome of a "personal" defense of the sort that Congress has plainly indicated should not be assertable against a bankruptcy estate or trustee.[23]

B. The Eleventh Circuit's ruling that Section 541 is so "unambiguous" as to prohibit consideration of its legislative history creates a split in the Circuits, and a departure from prior rulings by this Court, on that issue.

In the present case, however, the Eleventh Circuit refused even to consider the legislative history of Section 541, based on its conclusions (1) that the provision is "unambiguous," and thus any consideration of legislative history is not warranted, and (2) that the portion of the legislative history on which the Trustee relies pertains solely to Section 541(d) rather than Section 541(a).[24] Both of these conclusions are demonstrably incorrect, and conflict with both rulings by the other Circuit Courts and prior opinions of this Court.

---

[22] *In re Fuzion Tech.*, 332 B.R. at 232-233.

[23] *See, e.g., Exxon Corp. v. Oxxford Clothes, Inc.*, 109 F.3d 1070, 1078 n.11 (5th Cir. 1997) (equitable defenses are personal defenses); *Pyrodyne Corp. v. Pyroteronics Corp.*, 847 F.2d 1398, 1402 (9th Cir. 1988) (same); *Hrisomalos v. Smith*, 600 N.E.2d 1363, 1366 (Ind. Ct. App. 1992) (equitable defenses like unclean hands are personal defenses); *Resolution Trust Corp. v. Associated Gulf Contractors, Inc.*, 622 A.2d 1324, 1330-31 (N.J. Super. Ct. App. Div. 1993) (same); *Nomura Sec. Int'l, Inc. v. E*Trade Sec., Inc.*, 280 F. Supp. 2d 184, 196-97 (S.D.N.Y. 2003) (*in pari delicto* is analogous to the doctrine of unclean hands).

[24] *Laddin v. Edwards (In re PSA, Inc.)*, 437 F.3d 1145, 1150 (11th Cir. 2006); Appendix B at 18a-19a.

First, the plain language of Section 541 does not address *in pari delicto* or, for that matter, any defenses or their applicability to bankruptcy estates or trustees. Rather, the language defining "property of the estate"—inarguably among the most fundamental provisions of the Bankruptcy Code—is exceptionally broad, and its proper construction and application plainly warrant an inquiry into the legislative history of the statute.

Not surprisingly, therefore, courts have routinely looked to Section 541's legislative history for guidance in construing the broad language of the statute. For example, after noting in *Miller v. Shallowford Cmty. Hosp. Inc.*, that Section 541(a)(1) "broadly defines" the property of a debtor's estate to include "all legal or equitable interests," even the Eleventh Circuit looked to legislative history to determine which legal and equitable interests are included in the property of the estate.[25]

Indeed, both this Court and all of the Circuit Courts of Appeals have utilized legislative history to interpret Section 541.[26] Moreover—and although they missed or ignored the

---

[25] 767 F.2d 1556, 1559 (11th Cir. 1985) (citing S. REP. NO. 989, 95th Cong., 2d Sess. 82, *reprinted in* 1978 U.S.C.C.A.N. 5787, 5868 (the "Senate Report"); H.R. REP. NO. 595, 95th Cong., 1st Sess. 367, *reprinted in* 1978 U.S.C.C.A.N. 5963, 6323 (the "House Report") ("The legislative history [of 11 U.S.C. § 541 (a)(1)] indicates that [the] definition [of property of the estate] includes causes of action . . . ."). *See also Johnson, Blakely, Pope, Bokor, Ruppel & Burns, P.A. v. Alvarez* (*In re Alvarez*), 224 F.3d 1273, 1278 n.12 (11th Cir. 2000) (same); *T & B Scottdale Contractors, Inc. v. United States*, 866 F.2d 1372, 1376 (11th Cir. 1989) (citing to the Senate and House Reports in construing section 541(a)(1)).

[26] *See, e.g., United States v. Whiting Pools, Inc.*, 462 U.S. 198, 204-05 n.8-9 (1983) (relying on legislative history to observe that in enacting section 541(a)(1) "Congress intended a broad range of property . . . to be included in the estate"); *Tringali v. Hathaway Mach. Co., Inc.*, 796 F.2d 553, 560 (1st Cir. 1986); *Rodgers v. County of Monroe* (*In re Rodgers*), 333 F.3d 64, 69 (2d Cir. 2003) (per curiam); *L.R.S.C. Co. v. Rickel Home*

critical portion of it, and consequently reached the wrong result—even other Circuit Courts faced with the very issues raised in this case have looked to the legislative history for guidance in interpreting the scope of Section 541(a),[27] thus indicating, at least implicitly, that they considered the text of the statute sufficiently unclear and ambiguous to warrant such an analysis. The very fact that other Circuit Courts have reached a contrary conclusion not only indicates a split in the circuits on this issue, but also belies, by definition, the Eleventh Circuit's determination in this case that Section 541 is so plainly unambiguous as to make reference to the legislative history impermissible.[28]

Second, while courts have certainly used the above-referenced portion of the legislative history to interpret Section 541(d), this does not mean its application is limited to that section. In fact, *Collier on Bankruptcy* relies on this

---

Ctrs., Inc. (In re Rickel Home Ctrs., Inc.), 209 F.3d 291, 297 (3d Cir. 2000); *Shumate v. Patterson*, 943 F.2d 362, 363 (4th Cir. 1991); *Am. Nat'l Bank v. MortgageAmerica Corp. (In re MortgageAmerica Corp.)*, 714 F.2d 1266, 1274 (5th Cir. 1983); *Weingarten Nostat, Inc. v. Serv. Merch. Co., Inc.*, 396 F.3d 737, 742 (6th Cir. 2005); *In re Paeplow*, 972 F.2d 730, 737 (7th Cir. 1992); *Garner v. Strauss (In re Garner)*, 952 F.2d 232, 234 (8th Cir. 1991); *Computer Commc'n, Inc. v. Codex Corp. (In re Computer Commc'n, Inc.)*, 824 F.2d 725, 729 (9th Cir. 1987); *Sender v. Simon*, 84 F.3d 1299, 1305 (10th Cir. 1996); *United States v. Inslaw, Inc.*, 932 F.2d 1467, 1471 (D.C. Cir. 1991).

[27] *See, e.g., Sender*, 84 F.3d at 1285-1286; *R.F. Lafferty & Co.*, 267 F.3d at 356.

[28] *See, e.g., In re Southern Star Foods, Inc.*, 144 F.3d 712, 715 (10th Cir. 1998) ("The existence of a split in the circuits in the interpretation of [a statute] is, in itself, evidence of the ambiguity of the language."); *Allapattah Servs., Inc. v. Exxon Corp.*, 362 F.3d 739, 747 (11th Cir. 2004) ("While [a] statute's meaning may appear to be obvious to an individual reader, a court cannot responsibly declare language to be 'clear' when, as a matter of empirical reality, significant numbers of jurists have reasonable, good faith disputes over its meaning. A judicial fiat declaring a statute to be unambiguous does not make it so.").

excerpt from the Joint Statement to explain the scope of section 541(a)(1).[29] Further, numerous courts have cited this excerpt while analyzing Section 541(a)(1).[30] Moreover, the excerpt itself expressly states that it is setting forth the premise of Section 541(a)(1):

> Thus, *as section 541(a)(1) clearly states*, the estate is comprised of all legal or equitable interests of the debtor in property as of the commencement of the case. To the extent such an interest is limited in the hands of the debtor, it is equally limited in the hands of the estate except to the extent that defenses which are personal against the debtor are not effective against the estate.[31]

While this excerpt immediately follows a description of Section 541(d), the subsequent, explicit reference to subsection (a)(1) is much more general, referring not only to the kinds of defenses that are assertable against the trustee, but also to the kinds that are not. Accordingly, the excerpt not only is *not* exclusive to Section 541(d), it expressly applies *to* Section 541(a)(1).

In short, the district and appellate courts in this case construed Section 541 too narrowly. The legislative history of the statute is crystal clear that "property of the estate" in-

---

[29] 5 COLLIER ON BANKRUPTCY ¶ 541.04 (15th ed. rev. 2004).

[30] *See, e.g., In re Combustion Eng'g, Inc.*, 391 F.3d 190, 219 (3d Cir. 2004) (characterizing the excerpt from the Joint Statement as the "Legislative Statement" to section 541(a)(1)); *Huber v. Danning (In re Thomas)*, 147 B.R. 526, 534 (9th Cir. 1992) (Volinn, J., dissenting) (citing to the excerpt from the Joint Statement for the proposition that "the language of section 541 was intended to be generally applicable"); *In re Village Rathskeller, Inc.*, 147 B.R. 665, 671 (Bankr. S.D.N.Y. 1992) (reproducing the excerpt from the Joint Statement in explaining section 541(a)(1)); *In re S.W. Citizens' Org. for Poverty Elimination*, 91 B.R. 278, 281 (Bankr. D.N.J. 1988) (same).

[31] 11 U.S.C.A. § 541 note (West 2004) (Legislative Statements); 124 CONG. REC. 32,399 (1978) (emphasis added).

cludes the debtor's claims unencumbered by any personal defenses. Moreover, the Eleventh Circuit's conclusion that Section 541 is so "unambiguous" as to preclude consideration of that legislative history conflicts directly with prior rulings by this Court and the other Circuit Courts. Accordingly, the IRA Custodians' *in pari delicto* defense is inapplicable to the Trustee's claims in this case, and the Eleventh Circuit's erroneous and ill-founded ruling to the contrary should be reversed.

II. This Case Creates A Split In The Federal Courts On Application Of The *In Pari Delicto* Defense To RICO Claims Generally, And Presents That Issue To This Court For A Definitive Ruling.

The Eleventh Circuit's ruling in this case that the *in pari delicto* defense is applicable to RICO claims, as a general matter, is also in conflict with the conclusions reached by other federal courts on that issue. In evaluating the affirmative defense of *in pari delicto*, state law governs state law causes of action and federal law governs federal law causes of action.[32] Accordingly, where a cause of action arises under a federal statute like RICO, federal policies bear on the question of estoppel defenses like *in pari delicto*.[33] Based on these policies, numerous federal courts have held that the *in pari delicto* defense simply is not applicable to RICO claims in any case or context.[34] Other federal courts

---

[32] *See O'Melveny & Myers v. FDIC*, 512 U.S. 79, 84-85, 114 S. Ct. 2048, 2053 (1994); *Schacht v. Brown*, 711 F.2d 1343, 1347 (7th Cir. 1983).

[33] *See Schacht*, 711 F.2d at 1347 ("the cause of action here arises under RICO, a federal statute; we therefore write on a clean slate and may bring to bear federal policies in deciding the estoppel question").

[34] *See, e.g., Harper v. American Tel. and Tel. Co.*, 54 F. Supp. 2d 1371, 1380 (S.D. Ga. 1999) ("In considering the similar common law defense, *in pari delicto*, several courts have held that it is not applicable in federal

have determined that equitable defenses are inapplicable when a plaintiff's claims would further the compensation and deterrent objectives of RICO.[35]

Rather than following any of these authorities, however, and in the absence of conclusive guidance from this Court in the RICO context, the Eleventh Circuit in this case instead engaged in a protracted and tortuous analysis[36] of this Court's rulings in what it deemed to be analogous cases, involving federal securities and antitrust laws based on similar enforcement policies and protective principles.[37] Notwithstanding the fact that this Court declined to apply *in pari delicto* to the claims in both of those cases, moreover, the Eleventh Circuit drew ill-founded distinctions and, with no further basis in or reliance upon relevant case law, concluded that the defense *did* apply to the RICO claims in this case.[38]

The Eleventh's Circuit's opinion here is thus at odds with the conclusions reached by other federal courts on the appli-

---

RICO cases."); *In re National Mtg. Equity Sec. Litig.*, 636 F. Supp. 1138 (C.D. Cal. 1986).

[35] *See Schacht*, 711 F.2d at 1348-49, 1359-60 (conducting compensation and deterrent analysis to determine whether insurance company liquidator should be estopped from pursuing RICO claim against accounting firm, and concluding that liquidator was precisely the kind of plaintiff that should have right to pursue such a claim in order to fulfill the deterrent objectives of RICO).

[36] *Laddin*, 437 F.3d at 1152-1156; Appendix B at 22-30a.

[37] *Bateman Eichler, Hill Richards, Inc. v. Berner*, 472 U.S. 299, 310-11, 105 S. Ct. 2622, 2629 (1985) (*in pari delicto* defense is allowed in securities fraud case only if "preclusion of suit would not significantly interfere with the effective enforcement of the laws and protection of the public."); *Perma Life Mufflers, Inc. v. International Parts Corp.*, 392 U.S. 134, 140, 88 S. Ct. 1981, 1985 (1968) (refusing to recognize *in pari delicto* as a defense to an antitrust action in light of purposes of antitrust laws).

[38] *Laddin*, 437 F.3d at 1155-1156; Appendix B at 29a-30a.

cability of *in pari delicto* to claims arising under the RICO Act, and inconsistent with this Court's prior rulings in the analogous areas of securities regulation and antitrust. Plainly, the time is right for a definitive ruling by this Court on the precise issue of whether the *in pari delicto* defense applies to RICO claims as a general matter, and this case presents the Court with an opportunity to have the final, conclusive word on that unquestionably prevalent and significant issue.

III. The Results In This Case, And In The Prior Circuit Court Decisions Applying *In Pari Delicto* To Bankruptcy Trustees, Betray The Equitable Principles Embodied In The Bankruptcy Code And Conflict With The Manner—Accentuating Flexibility In The Service Of Equity Rather Than Rote Application—In Which This Court And The Other Federal Courts Have Consistently Directed Section 541 And Other Provisions Of The Bankruptcy Code To Be Administered.

Finally, in a case such as this one, the equitable principles embodied in the Bankruptcy Code preclude the application of an estoppel doctrine like *in pari delicto* to bar a suit by an innocent plaintiff in the nature of a bankruptcy trustee. The question is ultimately a matter of federal policy, and specifically, of the fundamental equitable principles underlying the Bankruptcy Code as a whole. In dismissing the Trustee's claims, the lower courts in this case refused to consider the post-petition removal of the wrongdoer (Edwards) and appointment of an innocent party (the Trustee) seeking recovery for the benefit of innocent investors and other creditors. The courts again felt bound by their conclusion that, under Section 541, defenses must be evaluated and rotely applied solely as they existed at the moment of the bankruptcy, no matter how little sense this may make under the circumstances, and regardless of the extent to which they had to ignore—or even

deny[39]—the inarguable factual realities before them. As demonstrated above, the legislative history of Section 541 does not support such a restrictive interpretation of the statute.

Further, federal courts, specifically including this Court, have historically recognized that rights at the moment of bankruptcy are not the sole determinant of what is property of the estate. Bankruptcy principles and policies play an important role in the analysis and can justify the consideration of post-petition events in order to insure an equitable result. In this regard, the Eleventh Circuit's decision in this case is flatly at odds with prior rulings by this Court. In *Segal v. Rochelle*, for example, this Court allowed a trustee to claim as property of the estate a tax refund for a taxable year that ended post-petition.[40] Permitting the consideration of the post-petition event (the ending of the tax year) for purposes of determining "property of the estate," the Court reasoned that the refund was "sufficiently rooted in the pre-bankruptcy past and so little entangled with the bankrupts' ability to make an unencumbered fresh start that it should be regarded as 'property.'"[41] In reaching this conclusion, the Court specifically stated that bankruptcy policy and purposes must

---

[39] Among the conclusions reached by the Eleventh Circuit in this case is the stunning assertion that the Trustee's "recovery under RICO [in this case] would not divest RICO violators of their ill-gotten gains, it would result in a wealth transfer among similarly situated conspirators." *Laddin*, 437 F.3d at 1155; Appendix B at 27a. This statement denies the simple reality of the situation, disputed by no one—that the actual perpetrators of any fraud within ETS had been eliminated, that the IRA Custodians were alleged to have violated RICO in their own rights, and that any recovery by the Trustee would inure only to the entirely innocent victims of the scheme.

[40] 382 U.S. 375, 380, 86 S. Ct. 511, 515 (1966). Notably, *Segal* is specifically referenced and approved in the legislative history of Section 541. 11 U.S.C.A. § 541 note (West 2004) (Revision Notes and Legislative Reports—1978 Acts); 1978 U.S.C.C.A.N. 5963, 6323-24.

[41] *Id.*

ultimately govern questions as to what is property of the estate.[42] Accordingly, this Court's focus in *Segal* was not on whether the right to the refund had fully vested at the moment of bankruptcy but, rather, on whether classifying the refund as property of the estate would encumber the bankruptcy policy of giving the debtor a "fresh start."[43]

In *Kokoszka v. Belford,* this Court likewise held that, in determining the scope of the term "property"—and its limitations—the "purposes of the Bankruptcy Act must ultimately govern."[44] The Court in that case concluded that a garnishment statute restricting the garnishment of wages to 25% could not limit the right of the bankruptcy trustee to treat the debtor's entire income tax refund as property of the estate.[45] Again, in its analysis, the Court considered whether the purposes of the Bankruptcy Act—to convert the estate of the bankrupt into cash and distribute it among creditors and to give the bankrupt a fresh start—would be served by including the entire tax refund within the property of the estate despite the applicability of the garnishment statute.[46]

Other federal courts have freely considered post-petition acts in applying other provisions of the Bankruptcy Code as well—all in service of the equitable purposes of the bankruptcy courts and Code. For example, when a claim against the debtor's fraudulent managers is brought by the Trustee under Section 548 of the Bankruptcy Code, a "better rule" prevails on the issue of imputing the manager's fraudulent

---

[42] *Id.* at 379, 515.

[43] *Id.* at 379-80, 515.

[44] 417 U.S. 642, 645, 94 S. Ct. 2431, 2433 (1974).

[45] *Id.* at 652, 2437.

[46] *Id.* at 646-47, 2434. *See also Page v. Edmunds*, 187 U.S. 596, 605-06, 23 S. Ct. 200, 203-204 (1903) (seat in stock exchange *held* property of the estate under Bankruptcy Act even though property was exempt under state law).

conduct to the bankruptcy trustee: it's not allowed. Why? Because it "would lead to an inequitable result"—the *in pari delicto* defense would serve "only to bar the claims of an innocent successor."[47] Finally, in the comparable arenas of antitrust and securities law, federal policy often dictates restrictions on the use of *in pari delicto*, requiring courts to carefully consider public policy implications before the defense is allowed.[48]

If, as rulings by the Circuit Courts have thus far indicated, Section 541 is to be the sole exception to the "equity over rote application" approach that this Court and others have consistently mandated for construction and application of the Bankruptcy Code, then this Court needs to say so, clearly and definitively, in this case. If an aberrant principle of bankruptcy law is to deny countless thousands of innocent creditors and investors their only potential source for any recovery whatsoever, then it needs to be a principle announced, justified in light of prior rulings and endorsed by the highest court in the land. The issue is one of critical, national importance, because Section 541—the section that defines property of a debtor's estate—is among the most fundamental provisions in the entire Code, and because the facts and equities presented here have been, and will continue to be, duplicated in every case involving a corporate debtor ren-

---

[47] *See McNamara v. PFS (In re The Personal & Bus. Ins. Agency)*, 334 F.3d 239, 241 (3d Cir. 2003). *See also PM Denver, Inc. v. Porter (In re Porter McLeod, Inc.)*, 231 B.R. 786, 794-95 (D. Colo. 1999) (refusing to apply *in pari delicto* defense under Section 544(a) where application of the doctrine would not be in the public interest); *Anstine v. Alexander*, 128 P.3d 249, 254-255 (Colo. App. 2005).

[48] *See Bateman*, 472 U.S. at 310-11, 105 S. Ct. at 2629 (*in pari delicto* defense is allowed in securities fraud case only if "preclusion of suit would not significantly interfere with the effective enforcement of the laws and protection of the public."); *Perma Life Mufflers*, 392 U.S. at 140, 88 S. Ct. at 1985 (refusing to recognize *in pari delicto* as a defense to an antitrust action in light of purposes of antitrust laws).

dered insolvent by the fraud of its principals. Unfortunately, and as exemplified in recent years by companies such as Enron and Worldcom, such cases are becoming only more and more prevalent.

In sum, while the relevant substantive law is important in determining the rights a party has under a federal statute, courts across the board recognize that the federal purposes and policies behind the statute ultimately govern the scope and extent of those rights. In the bankruptcy context, this means that post-petition acts may be considered when doing so would serve the higher cause of preventing inequitable results. Indeed, the Trustee is charged with marshaling the assets of the estate and distributing them in the best interests of the parties. The Trustee "is the last good person who can help the creditors and ensure that the loss is borne by those who caused it and not by innocent people."[49]

Accordingly, the post-petition replacement of Edwards with the Trustee in this case should be relevant (and controlling) to the *in pari delicto* analysis. Indeed, refusing to consider it has the ironic effect of turning the defense on its head—instead of preventing a wrongdoer from profiting from his wrong, the defense shields the wrongdoers from liability and punishes the innocent victims. The equitable policies governing the *in pari delicto* defense and underlying federal bankruptcy law preclude such a perverse result. As best articulated by Chief Judge Posner, writing for the Seventh Circuit in a receivership case:

> [T]he wrongdoer must not be allowed to profit from his wrong by recovering property that he had parted with in order to thwart his creditors. That reason falls apart now that [the wrongdoer] has been ousted from control of and beneficial interest in the corporations. The appointment of the receiver removed the wrongdoer from the scene.

---

[49] *In re Fuzion Tech.*, 332 B.R. at 234.

> The corporations were no more [the wrongdoer's] evil zombies. Freed from his spell they became entitled to return of the moneys—for the benefit not of [the wrongdoer] but of innocent investors—that [the wrongdoer] had made the corporations divert to unauthorized purposes.[50]

In other words, the doctrine of *in pari delicto* "loses its sting when the person who was *in part delicto* is eliminated."[51]

While at least one lower court has correctly applied this reasoning in the bankruptcy context,[52] the Eleventh Circuit in this case got it wrong, as have all of the Circuit Courts that have addressed the issue to date. In this case, and with one definitive ruling, this Court can correct those errors and set the lower federal courts on the right course on this seminal issue, once and for all.

---

[50] *Scholes v. Lehmann*, 56 F.3d 750, 754 (7th Cir. 1995).

[51] *Id.* at 755.

[52] *See In re Fuzion Tech.*, 332 B.R. 225. *See also R.F. Lafferty*, 267 F.3d at 361-63 (Cowen, J. dissenting). In fact, *In re Fuzion* is both the case most precisely on point and the only one in which a court has performed the appropriately thorough analysis—considering *all* of section 541's legislative history, the equitable principles governing the doctrine of *in pari delicto*, the equitable policies governing the Bankruptcy Code, and the policies underlying the applicable federal statute—and reached the correct result, concluding that "as a matter of law, the *in pari delicto* defense does not apply to the bankruptcy trustee." 332 B.R. at 236.

CONCLUSION

For all of the reasons set forth herein, Petitioner prays that a writ of certiorari issue to the United States Court of Appeals for the Eleventh Circuit.

Respectfully submitted,

ALLEN I. HIRSCH *
DARRYL S. LADDIN
FRANK N. WHITE
ARNALL GOLDEN GREGORY LLP
171 17th Street N.W.
Suite 2100
Atlanta, Georgia 30363
(404) 873-8500

* Counsel of Record

Attorneys for Petitioner, Darryl S. Laddin, as Trustee of the ETS Creditors' Litigation Trust